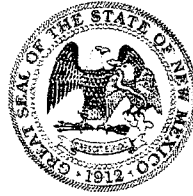


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June 28, 2007

**MEMORANDUM**

**TO:** Legislative Education Study Committee

**FR:** Peter van Moorsel *PvM*

**RE: WRITTEN REPORT: LFC AUDIT OF REGIONAL EDUCATION  
COOPERATIVES**

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After a request to the Legislature from the Regional Education Cooperatives (RECs) for a \$2.7 million appropriation to continue operating, the Legislative Finance Committee (LFC) performance auditors conducted a review of the RECs to determine the level of fiscal oversight provided by the Public Education Department (PED) and to determine how RECs operate, what services they provide to school districts, and the funding they receive. The review addressed applicable laws; PED and REC policies and procedures; financial audits of RECs for FY 04 through FY 06; and reimbursement submission payments. Also, the LFC performance auditors conducted interviews of PED and REC officials, and reviewed other documents and data provided during field visits to five RECs. The LFC report of the review is attached.

In their findings, the LFC auditors state that:

- PED does not consistently reimburse the RECS on a timely basis because of incorrect REC reimbursement submissions, PED processing delays, and difficulties implementing a new accounting system in the first quarter of FY 07.
- Beginning in FY 06, PED began administering federal flow-through funds on a twice-monthly reimbursement basis in order to comply with the federal *Cash Management Improvement Act*. As a result of this change, some RECs are experiencing cash flow

problems. (Prior to FY 06, PED flowed federal dollars directly to RECs in the form of either a one-twelfth allotment at the beginning of each month, or a quarterly request for cash.)

- The 2006 Legislature approved \$750,000 in cash flow assistance to the RECs to be repaid to PED by June 30, 2007. As of January 15, 2007, \$625,000 had been advanced to Raton REC #3, Las Vegas REC #4, Albuquerque REC #5, Ruidoso REC #9, and Truth or Consequences REC #10.
- Two RECs violated the New Mexico Constitution by incurring debt. Ruidoso REC #9 established a line of credit with a limit of \$300,000 to cover salaries and operations. During a 17-month time period the loan amount reached the maximum 20 times and was paid off six times. On February 9, 2007, Ruidoso REC #9 paid off and closed this line of credit. Raton REC #3 established a mortgage of over \$400,000 to purchase a building.
- Opportunities exist for improved PED oversight.

Recommendations of the LFC review include the following:

- The Legislature should consider extending the June 30, 2007 repayment deadline for the initial cash flow assistance appropriation; consider providing an additional \$1.05 million in nonrecurring funds to bring the cash assistance amount to \$1.8 million to mitigate the RECs' cash flow problems (the 2007 Legislature appropriated \$1.05 million for this purpose, see background section of this document); and consider the consolidation of smaller RECs with financial difficulties with larger RECs to take advantage of economies of scale and to reduce overall REC expenditures. The recommendation to consolidate RECs is in agreement with findings of an assessment of RECs by MGT of America in 2004. The MGT report also recommended consolidation of RECs to more economically serve the member school districts and provide a wider range of services.
- PED should streamline the review process of cash reimbursements; require the governing board of each REC to prepare a plan to address cash flow issues and submit such plans to PED for approval; and enhance oversight of the RECs through the designation of one internal FTE to oversee REC operations, services, planning, and cash reimbursements and conduct regular meetings.
- The RECs should ensure that reimbursement submissions are complete and correct; and ensure that the constitutional violations are rectified

Both PED and the RECs were given an opportunity to respond to the findings of the LFC review. In their respective responses:

- PED generally agreed with the findings and recommendations of the review. However, the department did take exception with the review's finding that PED experienced "difficulties learning a new accounting system in the first quarter of FY 07," stating that PED has processed more transactions with the new accounting system than any other agency.
- The REC executive directors disputed several of the review's findings and recommendations, including:

**Finding: Many of the smaller RECs are having financial difficulties because of declining school district membership and limited entrepreneurial opportunities in rural areas.**

Response: The REC response states that this finding is not accurate for all RECs, and adds that REC #3 is one of the smallest RECs in terms of enrollment, yet continues to be fiscally sound and continues to have a sufficient cash balance to meet the needs of both state and local initiatives because it utilizes the entrepreneurial opportunities in rural northeastern New Mexico.

**Finding: Consider the consolidation of smaller RECs with financial difficulties with larger RECs to take advantage of economies of scale and to reduce overall REC expenditures.**

Response: The REC response argues that consolidation of RECs was not in the initial scope of the LFC review. The response further states that, following the recommendation to consolidate RECs in the MGT report, consolidation was thoroughly discussed and debated among all stakeholders, including legislators, superintendents, administrators, education partners, and others. The RECs report that this discussion and debate resulted in an overwhelming consensus against consolidation of RECs.

**Finding: REC #9 violated the New Mexico Constitution by establishing a line of credit with a limit of \$300,000 to cover salaries and operations.**

Response: The REC response states that according to the REC #9 executive director, a line of credit was opened by REC #9 at the suggestion of PED and only after PED staff had contacted local bank officials. In addition, the REC #9 executive director reported that a PED official confirmed that she had contacted the local bank prior to the opening of the REC #9 line of credit; however, the PED official indicated that she couldn't recall whether she authorized the line of credit or not.

**Finding: Raton REC #3 established a mortgage of over \$400,000 to purchase a building.**

Response: The REC response states that the REC #3 executive director is currently working with International Bank to rectify the mortgage.

### **Background:**

In 1993, the *New Mexico Regional Cooperative Education Act* was enacted to permit the State Board of Education (now PED) to authorize the formation of RECs to provide education-related services. According to the statute, RECs are deemed individual state agencies administratively attached to PED.

According to PED, nine RECs currently serve 58 of New Mexico's public school districts and charter schools and other state-supported facilities, including juvenile justice sites statewide, the Children's Psychiatric Hospital, the Department of Corrections, and the Sequoyah Adolescent Treatment Center. (For a list of REC members, see Appendix A of the LFC report.) PED notes that the services offered by RECs vary. In addition to serving as administrators of some *Individuals with Disabilities Education Act* (IDEA) funds and providing technical assistance to

participating districts on special education issues, some REC's have expanded their operations as permitted by the act to provide services from sources such as:

- the federal *Drug-Free Schools and Communities Act of 1986*;
- the federal *No Child Left Behind Act of 2001* (NCLB) Reading First and Transition to Teaching initiatives; and
- the federal *Carl D. Perkins Act*.

No funding sources are currently required in regulation or statute for the operation of REC's. However, PED states that \$1.0 million in federal IDEA-Part B funds is set aside annually to be allocated equally among the REC's for infrastructure costs. For FY 07, the nine REC's currently in operation each received \$111,000 for these costs. PED reports that REC's manage all of the flow-through IDEA funds for their member districts and have agreements to allocate some of those funds to operate their offices. REC's may also support programs and operations through other state and federal grants and contracts.

In 2006, the Legislature appropriated \$750,000 in special nonrecurring funds to PED to provide temporary cash flow assistance for REC operations in FY 07. The appropriation language required that any advances be returned by June 30, 2007, but also stipulated that the appropriation would not revert at the end of FY 07, but would instead remain available for advances to the REC's through FY 08.

In 2007, as a result of the recommendation in the LFC review, the Legislature increased the total amount of funds available for advances to the REC's to \$1.8 million by appropriating an additional \$1.05 million, and extending through FY 09 the time that the 2006 appropriation would be available for advances to the REC's. The 2007 appropriation language gives PED more flexibility in advancing funds to the REC's, as follows:

- PED is allowed to advance funds to REC's that have submitted timely quarterly financial reports, are in compliance with state and federal financial reporting requirements, are otherwise financially stable, and have adequately justified a need for a cash advance;
- cash advances granted from this appropriation must be returned to PED by June 30, 2009; and
- these dollars shall remain available for additional advances to REC's.

SEE NOTEBOOK FOR  
COMPLETE REPORT

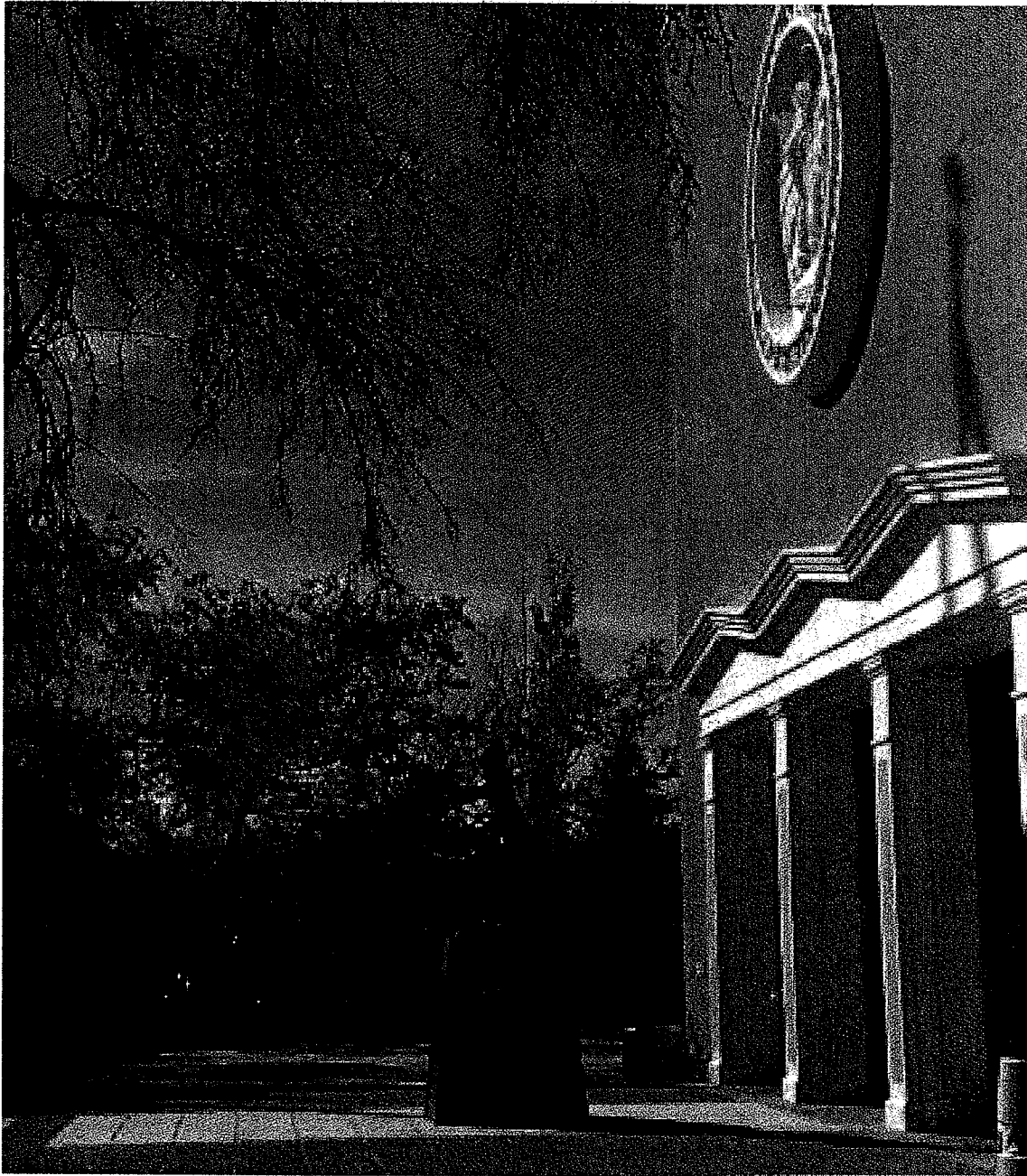
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Report  
to  
The LEGISLATIVE FINANCE COMMITTEE

JUN 21 2007

LESC



Public Education Department  
Review of the Regional Education Cooperatives  
May 2007

Report #07-13